Chapter

Corporate Governance: The Sustainability Quest

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Abstract

In recent times, the concept of corporate governance has become a topical interest to both academia and industry, the focus of attraction has mostly been on the need to understand its potency in advancing a corporation's ultimate interest, and hence the necessity for this study. This study aims to examine corporate governance. The study utilized a narrative literature review methodology to examine the concept of corporate governance, essence of corporate governance, scope of corporate governance, principles of corporate governance, internal corporate governance controls, external corporate governance controls, merit of corporate governance, and stewardship theory perspective to corporate governance. The study finally made postulations on the prospect of corporate governance.

Keywords: corporate governance, stewardship theory, sustainability

1. Introduction

The evolving of the concept of corporate governance started from the Greek term "kyberman" which denotes to guide, steer or govern; from which it transcends to a Latin concept "gubernare," and "governer" from a French perspective. It generally portrays the decision-making processes and execution strategies; nonetheless it connotation could change with regards to the peculiarity of an organization [1].

Cadbury [2] defines corporate governance (CG) as a structure by which organizations are controlled and directed, Obodo [3] posits that CG involves the balance of power with which the organization is directed, managed, supervised and held accountable. CG, to an extent, is a tool through which outside investors secure themselves against expropriations by the insiders and management [4]. Another competing definition is that CG is an interplay of the relationship between company management, shareholders, board, and auditors, etc. [5]; hence, it is ultimately about regimes of accountability [6]. The basis of CG does not end at how organizations are directed and managed but includes how to ensure and promote accountability and responsibility to all stakeholders; therefore, CG will always be in existence as long as the corporate structure is undermined, and the managers and investors experience conflict [7].

Ngozi and Raymond [8] posit that CG is perceived as having significant implications for the growth prospects of an economy, because best CG practice reduces risks for investors, attracts investment capital and improves the performance of organizations [9]. Effective CG is critical to securing corporate accountability, advancing the reliability and validity of financial information, and ensuring the efficiency and integrity of capital markets, with a positive effect on investor confidence [10].

CG in Nigeria is influenced by both internal and external factors comprising of various institutions and individuals charged with the responsibility to ensure effective management, control and accountability of public organizations [11]. The evolution and principles of the CG system in Nigeria were covered by the Companies and Allied Matters Act (CAMA) and improved further in the various Codes of Corporate Governance, the CG situation in Nigeria does not represent a complete lack or absence of structures, legislations and regulations rather, the ineffectiveness of the legislations and structures to effectively ensure compliance and enforcement [3]. CG can be identified through acceptable principles which consist of guidelines for decision-makers to enable them competently manage the economic and human resources in an open, accountable, transparent and lawful manner [12].

In recent times, unpleasant realities in the business world have questioned the credibility of CG. These unpleasant realities, as evidenced by the collapse of the stock market, uncovering of flagrant abuse of regulations practices, and high incidence of corruption in the economy [13]. Oyebode [14] posits that the massive fraud "cooking" of books in organizations not to mention insider dealings and compromised boards in many organizations, as well as spineless shareholders' associations', committees for audit and ineffective Annual General Meetings, imply the collapse of CG, and the necessity for a viable CG. Theses unpleasant realities were addressed via CG decisions (i.e. consolidation, mergers and acquisition, etc.) [15], the efficacy of the CG system in limiting these realities [16], have heightened the interest in understanding CG, and this the study aims to accomplish.

The remaining section of this paper will be divided into the following heading; methodology, concept of CG, essence of CG, scope of CG, principles of CG, internal CG controls, external CG controls, merit of CG, stewardship theory perspective to CG, and conclusion and prospect of CG.

2. Methodology

The narrative literature review methodology was utilized for this study. Its rationale is anchored on the significant scientific role it plays; as it is a critical element of most theses, empirical articles, book chapters, and grant proposals. It engages concepts in a much broader and abstract manner, and is most ideal when aligning diverse author's inputs, either for the objective of interconnection or reinterpretation [17]; it aids in understanding the body of knowledge on a specific concept, which offers valuable integration and overviews [18].

3. Concept of corporate governance

CG reveals the allotment of responsibilities and rights among diverse policy-makers in an organization (i.e. shareholders, managers, board members, etc.) and outlines the values, operation modes, and norms for making and executing decisions on the affairs of the organization [5]. CG also connotes the structure of norms, processes, systems and relationship through which authority is activated and engaged to optimally achieve the goals and objectives while monitoring performance and compliance in the organization [5]. Cochran and Warwick [19] define CG as an encompassing term that addresses particular issues resulting from interactions among management, shareholders, board directors and other corporate stakeholders.

4. Essence of corporate governance

OECD [5] notes that CG functions as a structure that protects the confidence of investors, advance capital market access and acceptance, and enhance the economic development of an organization. By explicitly postulation the operational mode and compliance checks for approved activities, the CG system decreases the operational cost and advance economic interest. The above makes CG essential, advantageous and practical for all forms and sector of an organization (i.e. multinationals, state-owned enterprises, domestic organizations, family-owned firms, and small businesses).

Notwithstanding the disparity in nations operation of CG with regards to the institutional, regulatory and legal environment, they possess a common aim; to define the rights, responsibilities and behaviors that are required of an organization's owners (the 'principals') and managers (the 'agents') for the business to operate successfully. Owners' connotes any person(s) who possess equity (i.e. shares) in the organization. Manager encompasses any person mandated to oversee the affairs of an organization by the owners' or board of directors of the organization.

When breaches in CG happen, they may be systemic, resulting from the negligence of duty or actual sabotage by employees. Nonetheless, the presence of a systemic failure (i.e. a global economic crisis) usually denotes a misalignment in the interest of the owners' and management; and this, an effective CG structure should have addressed before escalation.

5. Scope of corporate governance

OECD [5] posits that CG characteristically addresses procedures to manage, control, and decrease non-financial, operational, and financial risks by structuring the accountability, integrity, and transparency of an organization's management actors (i.e. board members, managers, employees and shareholders) at varying levels within an organization. Key scopes include:

i. Shareholders' rights: securing and facilitating the right and participation of the owner's in organization meetings, including voting on changes to the organization's structure (i.e. articles of incorporation) and major decisions of governance (i.e. membership of the board and members remuneration).

ii. Stakeholders' rights: recognition of the organization's impact on broader interest groups such as employees, customers and communities.

iii. Financial transparency: disclosure of the organization's operating and financial outcomes, the reward system for board members and senior management, and all associated information required to appraise organization and management performance.

iv. Proper accounting: duty to record all business transactions accurately (to avoid fictitious entries and off-the-book accounts), ensure internal sound controls (including the safe custody over assets) and employ proper accounting principles and techniques (i.e. liabilities, valuing organization, and assets). Usually, external accreditation may assist to guarantee the financial information validity being presented; via the activity of an independent party (i.e. with renowned integrity) assessment of the results.

v. Information sharing: obligation to present accurate, timely, and reliable information to the stakeholders, concerning the activities of the organization.

vi. Oversight: the creation of the board and organizational structures (e.g. committees and chairs) that ensure employees are responsible for and evaluate different dimensions of an organization's accountability and operations.

vii. Review: provision of evaluated output and reports on policy execution and effectiveness, the recommendation of changes where necessary.

While various institutional arrangements can be adopted for CG, an organization's board of directors is viewed as the framework's centerpiece; the board envisions leadership on tactical, strategic, and significant operational issues and is deemed as possessing a duty of care for an organization by setting the tone at the top and promoting a CG framework that covers all levels of the organization and risks.

6. Principles of corporate governance

OECD [5]; Ngozi and Raymond [8] posits that for CG to effectively function, the following principles must be present; transparency, accountability, and integrity of CG.

i. Transparency: ensuring that the benefits package of the board members and senior management team are made public; aligned to sustainable performance and decided by a non-executive independent director(s). Transparency International [20] supports government and institutional investors in their call for shareholder approval of the board members and senior management team reward packages (i.e. stock options, long-term incentives, and pensions). Organizations should publicly report on CG structures and anti-corruption systems, including their overall operations and performance.

ii. Accountability: Shareholder and stakeholder rights should include holding boards, owners and senior management accountable for their actions and respect the rights of owners. Minority shareholders rights should be safe and their voice encouraged. Effective participation and enacted rights aids in help in opposing policy and decisions that favor only the interest of the board and senior management teams; hence, discouraging corrupt actions or masked abuses.

iii. Integrity: the same CG standards should be applied across all units of an organization and in all countries where it operates. Good CG standards, rules and ethical principles should not be limited to the parent organization. Equally, organizations should be committed to improving CG standards in any alliance where they possess influence (e.g. consortia, joint ventures, suppliers, and agents). Exact board responsibilities must be apportioned to oversee CG as well as ethical and integrity issues. Transparency International [20] strongly advocates the establishment of independent remuneration and audit committees. Whistle-blowers should be secure, protected and encouraged, to avoid retaliation and victimization.

In supporting these principles of good CG, organizations should be willing to enact the key tools required to reduce risk, corruption, and enhance their zero tolerance for abusive actions. The optimal establishment, execution and restructuring of such a system will guarantee that corruption is neither a tolerable nor legitimate business coat.

7. Internal corporate governance controls

Sreeti [19] posits that internal CG monitors and controls activities; and executes corrective action to achieve organizational goals. This function includes:

i. Monitoring by the board of directors: directors' board, has a legal mandate and authority to recruit, sack, and reward executive management, secure capital invested. A regular meeting of the board ensures that potential issues are identified, brain-stormed, and solutions are decided. While non-executive directors are believed to be much autonomous, it may not result in much effective CG practices and may not advance performance. Nonetheless, the capacity of the board to supervise the organization's executives is anchored on its ability to access information. Executive directors have advanced knowledge of processes in the decision-making process and appraise top executive based on the value of their decisions that resulted in the statement of outcome for the organizations' financial and non-financial performance.

ii. Internal control processes and internal auditors: This encompasses policies executed by an organization's directors' board, the committee for audit, management, and employees to provide appropriate assurance of the organization accomplishing its goals. Internal auditors are employees in an organization who evaluate the design and execution of the organization's internal control process and the reliability and consistency of its financial reporting.

iii. Power balance: This implementation of power separation is encouraged in organizations; where distinct units check and balance one another's activity. One unit may recommend an organization-wide administrative change, the other unit could review the recommendation, and another unit may veto the recommendation, and yet another may evaluate the securing of interest of other stakeholders (i.e. customers, employees, shareholders).

iv. Remuneration: remuneration akin to performance-based is designed to correlate reward to employee performance. It could be in the cash form or non-cash form (i.e. shares, stock, etc.). These incentive schemes are mostly reactive with regards to the logic that it offers no avenue for preventing opportunistic conduct and mistakes, and may educe myopic behavior.

8. External corporate governance controls

Sreeti [21] posits that external CG controls involve the exercise of external stakeholders controls over the affairs of an organization. It includes:

i. Government regulations.

ii. Managerial labour market.

iii. Demand and evaluation of performance information (i.e. statements of finance).

iv. Media pressure.

v. Takeovers.

vi. Competition.

vii. Debt covenants.

9. Merit of corporate governance

Palia and Lichtenberg [22]; Black et al. [23], note the followings as benefits inherent in the rightful application of CG;

i. Ensures corporate success and economic growth.

ii. Maintains investors' confidence.

iii. Establishes a positive impact on the share price.

iv. Effectively minimizes wastages, corruption, risks and mismanagement.

Gompers et al. [24] maintain that good CG increases valuations and boost the profitability of the organization. Claessen et al. [25] note that better organizations frameworks benefit organizations through greater access to financing, lower cost of capital, better performance and more favorable treatment of all stakeholders. Donaldson [26] posits that good CG is important for increasing investor confidence and market liquidity. Frost et al. [27] state that improvements in CG practices ensure better disclosures in business reporting.

10. Stewardship theory perspective to corporate governance

The etymology of the stewardship theory is anchored in the field of psychology and sociology and its connotation according to Davis et al. [28] posits the protection and maximization of shareholders wealth via organization performance; this optimizes the steward's utility functions. In this analogy, stewards are organizations' management working for the interest of the shareholders. They secure and enhance profits for shareholders. Unlike the agency theory, the stewardship theory does not emphasize the view of individualism [29], but instead on the function of top executives as stewards, amalgamating their interest and goals with the organization. The stewardship view advocates that stewards are motivated and satisfied when organizational goals are attained.

Agyris [30] posits that the agency theory looks at an employee or people as an economic being, which suppresses an individual's ambitions. However, stewardship theory views the relevance of structures that equips the steward and offers optimal autonomy anchored on trust [29]. It emphasis the stature of employees or management to function autonomously, so that returns are maximized for the shareholders'. Hence, minimizing the costs focused on controlling and monitoring behaviors [28]. The stewardship concept suggests that a successful organization (not individual success) leads to happiness and hence motivate stewards [31].

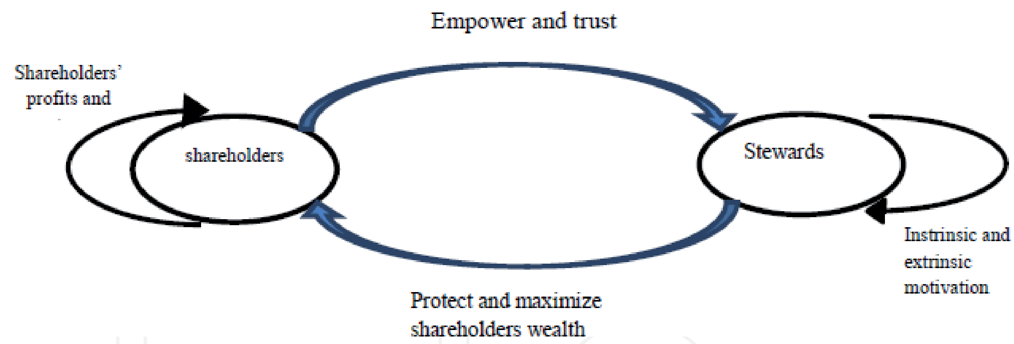

Figure 1.
The stewardship model. Source: [31].

Alternatively, Daly et al. [32] argue that to protect their reputations as decision-makers in organizations, management and directors need to optimally lead the organization to optimize non-financial and financial performance. Hence, Fama [33] posits that management and directors are likewise managing their jobs to be perceived as effective and result-oriented stewards of their organization, while, Shleifer and Vishny [34] insist that management return revenue to investors to foster a good reputation so they can re-enter the market for future finance. Peggy and Hugh [35] argue that unlike agency theory, stewardship theory helps in aligning the goals of managers and shareholders. When managers and shareholders' goals are aligned, organization performance is expected to increase as there is no conflict of self-interest (**Figure 1**).

11. Conclusion and prospect of corporate governance

An organizations' operations has impact that transcends the physical boundaries of their functioning, with influence on diverse issues of their environment (i.e. political, economic, legal, socio-cultural, etc.) which makes the role of their governance structural practices much strategic, and reinforces the need for sustainability. Today's CG structure and practice are constantly been scrutinized by diverse stakeholders as the easy resort to ethical, speedy, and sustainable enforcement of responsible corporate practices; this is necessitated by the negligence and slow pace of enacting legislative reform on such issues. Hence, CG when utilized as a tool possesses the capability to advance sustainable initiatives and engagement.

In prospecting it potency, the harnessing of this tool (i.e. corporate governance) demands a clear understanding of its potentials (i.e. concept of corporate governance, essence of corporate governance, scope of corporate governance, principles of corporate governance, internal corporate governance controls, external corporate governance controls, merit of corporate governance, and stewardship theory perspective to corporate governance, etc.). A key factor in this harnessing is the activity of stakeholders; corporation accountability must transcend beyond their shareholder to incorporate the stakeholders, and an effective framework should be streamlined to optimize the interactions of such engagement. Also, the GC actors of tomorrow must understand and have an experimental knowledge of their environment and the core of sustainability (i.e. today's action in exploring opportunity must not hinder the future availability and exploration of opportunities).

CG impacts the optimality of performance at the organizational and national level. Having explored the labyrinth of CG with a focus on the concept of CG, the essence of CG, the scope of CG, principles of CG, internal CG controls, external CG controls, the merit of CG, and stewardship theory perspective to CG, it is the author's opinion that CG plays a quintessential role in furthering the posterity and optimal sustainability of an organization's objectives as well as a nations' relevance at the global scene. Nonetheless, there is a need for optimizing the execution of CG practices via optimizing the flow of information, benchmarking best practices and standards, sustained commitment of all relevant stakeholders, and rewarding incentives to practitioners of CG practices.

The future of CG lies in their relevance today, and their ability to adapt to changing times as well as cover legal loopholes that undermine their potency. The practicality of that relevance for CG practices is strengthened in the involvement of relevant stakeholders in the formulation, enactment, and execution of such practices. Although the structuring, operating and controlling of an organization or nations' interest is not possible without the involvement of CG practices, CG practices can not be viable without the participation of relevant key stakeholders. The value of CG practices in today's organizations will continue to evolve as organizations are becoming agents of social re-engineers and not just economic transformers.

Conflict of interest

The authors declare no conflict of interest.

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